INVESTMENT SECURITIES—III.

BY FINANCIER.

General Mortgage Bonds.—Following their First, Second, Divisional and other Mortgage Bonds, many roads have issued their General Mortgage Bonds. A number of these securities were issued during the business depression of 1890 to 1896, when, as a result of the reckless railroad financing of the decade prior to 1890, many roads were forced into the hands of receivers.

The General Mortgage Bonds were secured by a general or "blanket" mortgage on all the property of the company, the lien being, of course, subject to the first or underlying bonds, many of which were not disturbed by the paring down of securities which the reorganization entailed. Most of the General Mortgage Bonds issued at this time bore four or five per cent. interest; and, as a result of the reorganization, holders of the secondary or junior mortgage bonds bearing six or seven per cent. interest were compelled to take General Mortgage Bonds, in part or in full, in exchange for their securities on which the road had been compelled to default. The result reduced the annual interest charges within the amount which it was anticipated the road could earn. In some instances, it was found possible to issue additional amounts of these General Mortgage Bonds, and with the funds thus obtained to rehabilitate the roads, the physical condition of many of which was deplorable.

Usually, the authorized issue of these General Mortgage Bonds was very large, and their term was made a long one—frequently a hundred years. Only a comparatively small proportion of the total amount authorized was put out at first. A large part of the issue would be reserved to take up or refund the underlying bonds as they matured.

A number of General Mortgage Bonds of some great systems are

now secured by a first lien upon important parts of the roads, as some of the First Mortgage Bonds which formerly preceded the General Bonds have matured, and have been paid off with the proceeds of the General Mortgage Bonds which had been reserved for that purpose. The General Bonds have thus become subrogated to the first lien of the bonds retired.

It is also usually provided in the General Mortgages that a certain amount, varying from $1,000,000 to $3,000,000 of bonds, may be issued each year to pay for improvements, the construction of branches, extensions, etc.

A typical issue of this class, although not created as a result of a reorganization, is found in the General Mortgage Gold Bonds of the Chicago, Milwaukee and St. Paul Railway, a part of which bear 3½ per cent. interest and a part 4 per cent. The total amount authorized is $150,000,000, but only $40,000,000 has been issued, the balance being reserved to take up Divisional and Branch Bonds having a prior lien, or to provide funds for improvements, extensions, etc. These bonds are now secured by a first lien on over 1,700 miles of road and are a junior lien on nearly all the balance of the system. The Chicago, Milwaukee and St. Paul General Mortgage Bonds are regarded as thoroughly high-grade securities, not only because they are in part First Mortgage Bonds, but also because the total indebtedness of the Chicago, Milwaukee and St. Paul Railway is very light in comparison with the value of its assets, and because the net earnings of the road are between three and four times the amount required to pay the bond interest.

The Atchison, Topeka and Santa Fé Railway General Mortgage Four-per-cent. Bonds, due in 1995, were authorized in 1895 as a result of the Reorganization Plan which terminated the receivership of the road in that year.

Of the $165,490,500 of bonds authorized, $146,634,500 are now outstanding, and they are secured by a first mortgage on more than 5,000 miles of road. Since the reorganization, the Atchison has developed into a road of great importance, and its General Mortgage Bonds rank well among investment securities. The net earnings are not only sufficient to meet the interest charges, but they exceed the amount required for this purpose by an ample margin.

The Erie General Mortgage Four-per-cent. Bonds of 1996 are

less conservative in character than the Atchison or St. Paul bonds above mentioned. They are secured by a first mortgage on only a few miles, while on important parts of the road they are preceded by no less than six prior liens.

Consolidated and Unified Mortgage Bonds.—Bonds issued under Consolidated and Unified Mortgages are very similar to the General Mortgage Bonds. Usually, the total authorized issue is a large one and they run for a long period. As the underlying bonds mature, they are paid off by issues of the Consolidated or Unifying Bonds reserved for that purpose, the bonds being so named because many comparatively small debts are thus consolidated or unified.

Consideration of General, Unified and Consolidated Mortgage Bonds as Investments.—The fact that the total amount of General Mortgage Bonds outstanding is usually large—frequently exceeding $100,000,000—is in one sense an advantage to the investor because, as a result, there is, under almost any conditions, an active market for these issues. They are listed on most of the large Stock Exchanges in this country and some of them on some of the European Exchanges. They become widely distributed among bond-buyers; and, as the number of investors interested in them increases, the demand for them broadens. They may be at any time immediately converted into cash; and, as sales of the active issues occur on the Exchanges almost daily, one knows from the quotations which are published in the papers of all the large cities just what his bonds are worth. On the other hand, the fact that $1,000,000 or more of the bonds may be issued each year is regarded as a disadvantage by many investors. The influx of such a large amount of new bonds into the market may depress the prices. However, it may be said that the railroads, unless they can obtain a fair price for their securities, frequently withhold them from sale, and, too, as the bonds usually appear through the medium of a large banking firm, their distribution is accomplished without unduly affecting the markets. Nevertheless, careful investors favor bonds secured by a "closed mortgage"—that is, by a mortgage all the bonds authorized by which are outstanding and in the hands of the public. There is no occasion for apprehension, in the case of such a security, that the exigent needs of a road for funds, or other causes, will precipitate the throwing upon the market of a large block of the bonds for whatever price

they will bring. The demand for bonds, secured by a closed mortgage, is usually great enough to absorb, at fair prices, whatever sales may be made by investors.

First and Refunding Mortgage Bonds.—The First and Refunding Mortgage Bonds are in many respects similar to the General Mortgage Bonds. Most of them bear 3½ or 4 per cent. interest and run from thirty to fifty years. Several large issues of this class of security made their appearance three or four years ago, their creation being a result, in some respects, of the very prosperous business which the railroads were enjoying at that time.

The panic of 1893, as stated above, had resulted in a large number of railroad bankruptcies and reorganizations. The insolvency of a number of roads was due to the fact that many of them were extravagantly bonded; and, when business decreased, with the years of depression following 1893, they were unable to meet the interest on their obligations. Following this period of adversity, however, the roads have been, generally speaking, conservatively managed. Generous appropriations for rehabilitation and improvement have been made from earnings, and, as a result, the credit of our railroads in general has largely improved.

Following 1900, however, the roads found themselves without facilities for handling the traffic which was pressed upon them. They needed additional mileage of double track, new equipment, larger terminals, etc. It also happened that there were a number of high-rate obligations maturing at that time, and it became necessary to refund them. Our general financial situation was exceptionally strong and large funds of capital were available for investment. The railroads took advantage of the situation by creating these First and Refunding Mortgage Bonds. They not only managed to refund the bonds maturing at that time and to make provision for other issues becoming due, but also made the bonds provide funds for other purposes. Our banks and bankers were in an easy position, and had no difficulty in financing an issue of from $50,000,000 to $100,000,000, because they found the public ready to absorb these Refunding Bonds at a comparatively low rate of interest. Inasmuch as many of the maturing bonds were secured by a First Mortgage, the new Refunding Bonds—through the issuance of which the maturing bonds had been redeemed—became partly a First Mortgage Bond. If that part of the road on which they are a first lien is an essential part of the

system and the amount of the issue is not too heavy, the fact that the bonds are secured in part by a First Mortgage makes them attractive to those who favor conservative investments.

But, besides providing for the redemption of maturing bonds, the Refunding Mortgages usually provide for the issuing of bonds for other purposes. Under certain restrictions, an amount of bonds may be issued for extensions and improvements, and in some mortgages a part of the authorized issue may be floated to pay for stocks or securities which the issuing road may purchase. As an instance, the Chicago, Rock Island and Pacific Railway Company issued a part of its First and Refunding Bonds to finance the purchase of $10,000,000 of Chicago and Alton stock. So the mortgage securing these bonds is not purely what its name implies, *i. e.,* a First and Refunding Mortgage.

These First and Refunding Mortgage Bonds are similar to the General Mortgage Bonds in having a broad and active market. Associated with the bankers who were successful in floating large issues of these securities were a number of European banks and banking firms. As a result, the issues have not only a national, but an international, market. Some of them are listed in New York, London, Frankfort, Berlin and Amsterdam. It should be noted that there is a disadvantage in this world-wide market. A financial depression in any one of the foreign centres where the bonds are held may result in low prices for the bonds there, and as quotations in all markets must remain approximately equivalent, may depress the American markets. But a broad distribution of bonds is generally regarded as a point in favor of the issue. It means a larger demand for the securities than could be found in any one market, and therefore greater stability of prices under all conditions.

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